No. 14837

United States
COURT OF APPEALS
for the Ninth Circuit

THE FIRST NATIONAL BANK OF PORTLAND, a National Banking Association,

Appellant,

vs.

FRANK A. DUDLEY, Trustee in Bankruptcy of the Estate of Northwest Variety Wholesale, Inc.,

Appellee.

BRIEF OF APPELLANT

Appeal from the United States District Court for the District of Oregon.

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Appeal from the United States District Court for the District of Oregon.

STATEMENT OF PLEADINGS AND JURISDICTION

Appellant is a national banking association engaged in the general banking business in the State of Oregon and, for the purpose of convenience, will be hereafter referred to as the Bank. Northwest Variety Wholesale, Inc., an Oregon corporation, is in bankruptcy, and will be hereafter referred to as the Bankrupt. Respondent is the Trustee in Bankruptcy of this bankrupt estate and, also for the purpose of convenience, will be hereafter

referred to as the Trustee. At the time of its adjudication as a bankrupt, which was July 13, 1953, the Bankrupt maintained a general commercial account with the Bank and was indebted to the Bank upon a matured obligation. After the petition in voluntary bankruptcy was filed the Bank exercised its right of set-off and later filed with the Trustee its claim for the balance owing to it.

The Trustee filed his objection to the claim, alleging that the right of set-off was improperly exercised, and praying that the Bank be required to pay the sum set off to the Trustee as a prerequisite to the allowance of its claim. The Bank filed its answer to these objections asserting the validity of its set-off, alleging that it was properly exercised and praying that its claim as previously filed be approved.

The matter came on for hearing before the Honorable Estes Snedecor, Referee in Bankruptcy. Testimony was introduced and arguments made with the result that on February 15, 1955, the Referee made and entered his Findings of Fact and Conclusions of Law and, based thereon, his Order Denying the Claim.

A Petition for Review by the District Judge of the Order of the Referee, pursuant to the provisions of United States Code, Title 11, Section 67, was timely filed. The issues raised in the Petition for Review were considered by the District Court and an Order Affirming the Order of the Referee was entered on June 6, 1955. Timely appeal from the Order of the District Court was made on June 23, 1955, pursuant to the provisions of United States Code, Title 11, Sections 47 and 48.

STATEMENT OF THE CASE

In July of 1946, the Bankrupt, then doing business under the name of Northwest Buyers, opened a general commercial account with the Bank. This is the same account, unchanged in any respect, that was in existence at the time of the bankruptcy, and the balance in this account at that time is what was offset by the Bank. At no time was there any special arrangement of any kind concerning the account or the manner in which or the purposes for which it was to be maintained, nor was there any special understanding concerning the funds to be deposited therein or withdrawn therefrom. The account was always subject to the unrestricted check of the Bankrupt.

On October 11, 1952, the Bank loaned the Bankrupt the sum of $22,000.00 evidenced by an unsecured promissory note payable thirty days after date. On the date the note became due and until the date of the conference to which reference is hereafter made there were sums on deposit in the Bankrupt's account ranging from approximately $7,000.00 to approximately $11,000.00, but never less than $7,000.00. The Bankrupt made deposits in and drew checks on the account in the same manner and with approximately the same activity after the date of the conference to which reference is hereafter made as it had been from its opening until that date.

Some time during December of 1952, but prior to December 15th, Mr. David E. Ankrom, Secretary-Treasurer of the Bankrupt, and Mr. Arthur B. Baines, attor-

ney for the Bankrupt, called at the branch office of the Bank wherein the Bankrupt's account was maintained and informed Mr. Arthur W. Lynn, Vice President and Manager of this Branch, that the company was in financial difficulty. During this conference the representatives of the Bankrupt stated that it would like to arrange for the payment of its existing indebtedness in quarterly installments over a 12-month period. Mr. Lynn replied that this arrangement would not be acceptable to the Bank but that, if the indebtedness were paid in ten equal monthly installments commencing on January 15, 1953, the Bank would defer any action to recover the balance owing on the defaulted obligation so long as the installments were promptly paid, but not otherwise. Pursuant to this understanding, installments were paid in the months of January, February, March, April and May of 1953. No payment was made in either June or July.

On July 13, 1953, the Bankrupt filed its Petition in Bankruptcy. On July 14, 1953, after the Bankrupt had defaulted in the payment of the June installment and after it had filed its petition in bankruptcy, the Bank charged the account of the Bankrupt with the sum of $2889.14, which was the balance then credited thereto, and credited the same upon the note of the Bankrupt owing to the Bank, leaving a balance of $8184.19 which is the amount of the Bank's claim filed in this bankruptcy proceeding.

The primary question on this appeal involves the right of the Bank to exercise its right of set-off in this

manner. This, in turn, presents the supplementary questions of whether or not, under the circumstances involved in this case, this right has been waived or the Bank is for any reason estopped from asserting it.

SPECIFICATION OF ERROR

This is an appeal from the Order of the District Court affirming the Order of the Referee in Bankruptcy denying the claim of the Bank. The District Court did not state any Finding of Fact or Conclusion of Law either in his opinion or in the Order affirming the Order of the Referee. In his Opinion the Court indicated that it would not be inappropriate for the Bank to take an appeal to this Court, and it is assumed, therefore, that the conclusions of the District Court were similar to those of the Referee. Consequently, for the purpose of presenting the issues raised in this matter to this Court, the more detailed Findings of Fact and Conclusions of Law of the Referee will be considered as having been Findings and Conclusions of the District Court. Assuming, therefore, that the Findings and Conclusions of the District Court were the same as those of the Referee, the Bank, as the Appellant, asserts that the Court erred in the following particulars:

1. The Court erred in concluding as a matter of law, based upon the Findings of Fact, that the Bank waived its right of set-off.

2. The Court erred in concluding as a matter of law, based upon the Findings of Fact, that the Bank

so conducted itself as to be estopped to assert its right of set-off.

3. The Court erred in concluding as a matter of law, based upon the Findings of Fact, that at the time of the exercise of the right of set-off, the bank account maintained by the Bankrupt with the Bank had so acquired the characteristics of a trust fund that it could not be used in set-off.

4. The Court erred in concluding as a matter of law, based upon the Findings of Fact, that the claim of the Bank should be disallowed unless the sum of $2889.14, which was the amount set off by the Bank, should be surrendered to the Trustee.

5. The Court erred in not concluding, as a matter of law and based upon the Findings of Fact made by it, that the Bank was in all respects authorized to exercise its right of set-off in the manner in which it did and that the claim of the Bank should accordingly have been allowed.

ARGUMENT

Proposition I.

A creditor has the right to set off a debt owing by it to the bankrupt against a debt owing by the bankrupt to it; and, if the parties do not effect the set-off prior to bankruptcy, it is the duty of the trustee to do so after the bankruptcy.

11 U.S.C.A., Sec. 108;
Studley v. Boylston National Bank, 1913, 229 U.S. 523; 57 L. Ed. 1313;

Continental & Commercial Trust & Savings Bank v. Chicago Title & Trust Company, 1912, 229 U.S. 435; 57 L. Ed. 1268;
In re Field Heating and Ventilating Co., Inc., 7th Circuit, 1953, 201 F. 2d 316.

The applicable statute is 11 U.S.C.A., Sect. 108. It contains the following provision:

> "a. In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid."

Subsection (b) of this statute provides two circumstances where the set-off will not be allowed. The first is of a claim that is not provable against the bankrupt's estate, and the second is where the claim is purchased by or transferred to the creditor with a view to his obtaining a preference. It is not contended that the set-off exercised by the Bank in this case should be denied for either of these reasons.

The case of *Studley vs. Boylston National Bank of Boston,* 1913, 229 U.S. 523, 57 L. Ed. 1313, is noteworthy particularly for the discussion by the Supreme Court of the United States of the principle of set-off and for the expression of the attitude of the Supreme Court that it is a right existing at common law, expressly preserved by statute, and not lightly to be circumscribed or restricted.

The case involved the Collver Tours Co., hereafter called the "Company", which was in the business of conducting world tours. In 1907 it opened a general

commercial account with the Boylston National Bank of Boston, hereafter called the "Bank", with which it subsequently did all its banking business. In 1909 it established a line of credit of $25,000.00. In early 1910 the Bank was advised that the Company was in some financial difficulty. The Company's officers made suitable explanation, and the Bank made an additional loan of $5000.00 to it, increasing the total outstanding obligations of the bankrupt to the Bank to $30,000.00. This was shortly thereafter reduced to $25,000.00, represented by five $5000.00 notes, maturing respectively on September 12, 20, 30 and October 3 and 14 of 1910. The three notes due in September were paid as they became due by check drawn by the Company on the Bank. On October 3 the Bank offset sufficient of the Company's commercial account to pay the note then due, and it did the same thing on October 14 with the note due on that date. At the date of the last set-off there was approximately $19,000.00 left in the account.

On December 16, 1910, the Company filed a petition in bankruptcy. The trustee claimed that $22,500 of the payments made in the four months preceding the filing of the petition operated to give the Bank a preference. It was found that the deposits were honestly made in the regular course of business and without any intention of creating a preference. The set-off was allowed.

After reciting the facts of the case and quoting that portion of the Bankruptcy Act which is hereinabove set forth, the court continued with the following discussion of the right of set-off (229 U.S. at page 528, 57 L. Ed. at page 1316):

"That section did not create the right of set-off, but recognized its existence, and provided a method by which it could be enforced even after bankruptcy. What the old books called a right of stoppage—what business men call set-off—is a right given or recognized by the commercial law of each of the states, and is protected by the bankruptcy act if the petition is filed before the parties have themselves given checks, charged notes, made book entries, or stated an account whereby the smaller obligation is applied on the larger.

"The banker's lien on deposits, the right of retention and set-off of mutual debts, are frequently spoken of as though they were synonymous, while in strictness, a set-off is a counterclaim which the defendant may interpose by way of cross-action against the plaintiff. But, broadly speaking, it represents the right which one party has against another to use his claim in full or partial satisfaction of what he owes to the other. That right is constantly exercised by business men in making book entries whereby one mutual debt is applied against another. If the parties have not voluntarily made the entries, and suit is brought by one against the other, the defendant, to avoid a circuity of action, may interpose his mutual claim by way of defense, and if it exceeds that of the plaintiff, may recover for the difference. Such counterclaim can be asserted as a defense or by the voluntary act of the parties, because it is grounded on the absurdity of making A pay B when B owes A. If this set-off of mutual debts has been lawfully made by the parties before the petition is filed, there is no necessity of the trustee doing so. If it has not been done by the parties, then, under command of the statute, it must be done by the trustee. But there is nothing in 68a which prevents the parties from voluntarily doing, before the petition is filed, what

the law itself requires to be done after proceedings in bankruptcy are instituted.

"The bank was indebted to the Collver Company as a depositor some $54,000 for money deposited in good faith in the usual course of business, and with no purpose of enabling the bank to secure the right of set-off. The Collver Company, on the other hand, was indebted to the bank $25,000 on notes maturing at various dates. These were mutual debts, and if, on the date the first note became due, the Collver Company had failed to pay it, the bank could have enforced its banker's lien or its right of set-off, by applying $5,000 of the deposits in payment of the note which matured that day, and so on as each of the other notes became due. It cannot have been illegal for the parties on September 12, 20, 30, October 3 and 14, to do what the law would have required the trustee to do in stating the account after the petition was filed on December 16, 1910. No money passed in either instance; for, whether the checks for $5,000 were paid or note for $5,000 was charged was, in either event, a book entry equivalent to the voluntary exercise by the parties of the right of set-off.

"The bankruptcy act recognizes this right, and it cannot be taken away by construction because of the possibility that it may be abused. The remedy against that evil is found in the fact that the trustee is authorized to sue and recover if it is shown that after insolvency the money was deposited for the purpose of enabling a bank or other creditor to secure a preference. But to deny the right of set-off in cases like this would in many cases make banks hesitate to honor checks given to third persons, would precipitate bankruptcy, and so interfere with the course of business as to produce evils of serious and far-reaching consequence.
"Affirmed."

This case established the policy to be followed by the courts in dealing with the right of set-off. It emphasized that the statute did not create a right in derogation of

the common law, and therefore under the acknowledged principles of statutory construction to be strictly construed, but rather that it was a codification of existing law, and to be liberally construed to effect its purpose. (50 Am. Jur., Statutes, Sections 345, 346 and 402). The Court recognized that to construe the statute so as to restrict the right would result in the precipitation of bankruptcies which might otherwise be avoided, by discouraging creditors from entering into extension agreements or other work-out arrangements with their debtors, and that this is contrary to the purposes of the bankruptcy statutes. The Court further specifically stated that the remedy for abuse of the set-off lies in the obligation of the trustee to sue and recover the amount of any credit created by the bankrupt for the purpose of effecting a preference, not in imposing limitations and restrictions on it; and that the set-off of mutual debts and credits is the right of the creditor and the obligation of the trustee, save only in exceptional circumstances.

In the case now before this Court, the Referee found, and it is conceded by the parties, that the Bankrupt filed its petition in bankruptcy on July 13, 1953; that on that date the Bankrupt owed the Bank $11,000.00 on an unsecured promissory note; that the Bankrupt had had on deposit with the Bank in its commercial account the sum of $2889.14; and that on July 14, 1953, the day after the petition in bankruptcy was filed, the Bank set off the sum of $2889.14 of its debt owing from the Bankrupt against the balance in the Bankrupt's account. Assuming, without conceding, that the extension granted by the Bank was such as to give the Bankrupt's debt the status

of an unmatured obligation, it is well settled, and we are not advised of any contrary authority, that the right of set-off is equally applicable to matured and unmatured debts when exercised after the petition in bankruptcy has been filed. Remington on Bankruptcy, Section 1472; Collier on Bankruptcy, 14th Ed., Vol. 4, Section 68.10. On the fact alone of the mutual obligations of the Bank and the Bankrupt each to the other, the statute and the cases to which reference is hereinabove made require that the one obligation be set off against the other.

It is also conceded that at the time the Bank granted the conditional extension of time described in the Referee's Order Disallowing Claim the Bank could have exercised its right of set-off against the then balance in the account. This was an amount considerably greater than that in the account at the time the right was actually exercised. Mr. Baines, attorney for the Bankrupt, testified that if the Bank had not granted this conditional extension, bankruptcy would have then immediately ensued (Transcript of Record, page 41). This is exactly the result the United States Supreme Court foresaw, and decried, in the case of *Studley vs. Boylston National Bank of Boston,* 1913, 229 U. S. 523, 57 L. Ed. 1313, to which reference is hereinabove made.

Unless, therefore, the Bank is held to have lost its right of set-off merely because, instead of exercising the right immediately, it granted the Bankrupt an opportunity to work out its difficulties, subject only to the condition that the obligation of the Bankrupt owing to the Bank be paid in ten equal monthly installments—a

condition to which the Bankrupt agreed and which it did not keep—then the Bank most certainly had that right when it was exercised in July, after the breach of the condition by the Bankrupt and after the filing of the petition in bankruptcy.

We respectfully submit that the Findings of Fact do not paint an extraordinary situation bespeaking of waiver, estoppel or trust fund. On the contrary, there is not, in the Findings of Fact or evidence, any possible basis for the contention that the granting of such a conditional extension constituted either a waiver of the right or was conduct such as to estop the Bank from exercising it. Any such rule would necessarily require banks to refuse any request for an extension of time or other indulgence if there was any possibility of bankruptcy ensuing; and this, in the words of the United States Supreme Court, "would precipitate bankruptcy and so interfere with the course of business as to produce evils of serious and far-reaching consequence". *Studley vs. Boylston National Bank of Boston,* 1913, 229 U.S. 523, 57 L. Ed. 1313.

It is important at this juncture to remember that the extension made by the Bank was a conditional one, that it would not press for immediate payment of the obligation owing it "providing that the monthly payments of ten per cent were made", (Transcript of Record, page 18, paragraph No. 5); and that set-off was not in fact made until July 14, 1953, after the Bankrupt had breached this condition by failing to make the June payment and after it had filed its petition in bankruptcy.

The statute and cases initially require that the mutual obligations of the Bank and the Bankrupt each to the other be set off one against the other. If this mandate is not to be followed, the burden is on him who would defy it to justify his action. The Trustee, in fulfillment of this obligation to show why this statutory requirement should be ignored, has asserted that the Bank is estopped to exercise it, that the Bank has waived it and that the bank account maintained by the Bankrupt was in reality a special account and partook of the nature of a trust account. Each of these contentions will be discussed in detail, but in considering them it should be remembered that the burden is on the Trustee to establish the truth of his assertions; not on the Bank to establish that they are false. We submit that, as the facts and discussion will show, the Trustee has utterly failed to show any facts or any reason why the clear and unequivocal mandate of the statute should not be followed. On the contrary, all of the facts and evidentiary material before this Court support the Bank's exercise of its right and its demand that its claim be allowed.

Proposition II.

The Bank's conduct was consistent in every respect with its assertion of its right of set-off. There was no misrepresentation or breach of duty upon which an estoppel might be based. There was no clear and unequivocal conduct evidencing a waiver.

> 19 Am. Jur., Estoppel, Sec. 34 and 36;
> 31 C.J.S., Estoppel, Sec. 59 and 61;
> Remington on Bankruptcy, Vol. 4, Sec. 1442;

Germania City, etc., Bank vs. Loeb, 188 F. 285; appealed; appeal dismissed 58 L. Ed. 470;
In re Myers, 99 F. 691;
Chassen vs. United States, 1953, 2nd Circuit, 207 F. 2d 83.

Equitable estoppel is generally defined as the principle whereby a person is precluded from stating the truth, and arises where such person has by his actions, representations or admissions induced another to believe that certain facts exist and such other rightfully relied on the acts, representations or admissions and would be prejudiced by permitting the party to assert the truth. It requires an act, representation or admission, or silence when there is a duty to speak, rightful reliance by another and prejudice to such other by assertion of the truth. Without the concurrence of all three elements there is no estoppel.

19 Am. Jur., Estoppel, Sec. 34;
31 C.J.S., Estoppel, Sec. 59.

There is nothing in the findings of fact, or in the transcript, that supports the conclusion of law that the Bank is estopped to assert its right of set-off. The extension of time granted by the Bank, as found by the Referee, was that it would not press for the immediate payment of the obligation owing it, "providing that the monthly payments of ten per cent were made." (Transcript of Record, page 18, paragraph No. 5). There is no contention, nor is there any evidence, that any other representation was made by the Bank at any time to any person. Thus the first requirement of an estoppel is not present, and, without a misrepresentation of

some kind, there can be no estoppel. Also there is no evidence of any reliance by any party on any conduct of the Bank and there is no evidence that any person changed his position to his prejudice in reliance upon any conduct of the Bank. In short, there is no evidence that will support any of the three required elements of estoppel.

Waiver has been defined as the intentional relinquishment of a known right. It has as its basic requirement some clear and unequivocal conduct unmistakably evidencing an intention to relinquish a particular right.

> 19 Am. Jur., Estoppel, Sec. 36;
> 31 C.J.S., Estoppel, Sec. 61;
> Remington on Bankruptcy, Vol. 4, Sec. 1442.

In the case before this Court the Referee found that the Bank had stated it would refrain from pressing the Bankrupt "for immediate payment in full of the indebtedness due it, providing that the monthly payments of ten per cent were made." (Transcript of Record, page 18, paragraph No. 5). The strongest construction against the Bank of which this is subject is that the Bank could not press for immediate payment of the obligation for so long as the payments of ten per cent per month were made. If it is so construed, it is still true, and the Referee so found, that the Bankrupt did not make the payment required by it to be made on June 15, 1953 and, further, that the Petition in bankruptcy was filed on July 13, 1953, the day before the set-off was made. The Bank had every right under the extension as found by the Referee to set off the balance in the Bankrupt's account on July 14, 1953, the date the right was exercised.

Further, it was the understanding of Mr. Lynn, the is not present, and, without a misrepresentation of Vice President and Manager of the Livestock-Kenton Branch of the Bank, that, if he considered the Bankrupt's condition to be acceptable each month, he would accept the tendered monthly payment (Transcript of Record, p. 63); and that he could, at any time he saw fit, proceed to enforce collection of the full balance of the obligation then owing from the Bankrupt (Transcript of Record, p. 68). These are not the ingredients of an "intentional relinquishment of a known right". An example of waiver as applied in bankruptcy is *In re Myers,* 99 F. 691, where the bankrupt owed the bank $5000.00 on an unmatured debt. The bankrupt had a commercial account of $777.00 with the bank at the time of his bankruptcy, and at that time the bank transferred this commercial account into the name of the trustee and filed its proof of claim for the full amount of $5000.00. Thereafter the bank filed a petition for leave to amend its proof of claim to set off the sum of $777.00, and filed a new claim for $4223.00. The referee denied the petition and the Circuit Court reversed. The court observed that a waiver is an intentional relinquishment of a known right, and that there is no waiver where there has been a mistake of either law or fact. The petition averred that there had been a mistake both of law and of fact in that the cashier did not know he had the right of set-off at the time he filed the original claim for $5000.00, and that there was some indication that he had not been advised of the balance of the outstanding obligation. The court continued that no one had been prejudiced, no one had changed his position so

that the allowance of the petition should be denied, and that therefore the petition and the set-off should be allowed.

In addition to the requirement that there must be an intentional relinquishment of a known right, the courts have stated that, at least with reference to bankruptcy matters, a "waiver" may be retracted unless someone has relied on it to his prejudice. The court indicated this to be true in *In re Myers,* 89 F. 691, and it was reiterated in *Chassen v. United States,* 1953, 207 F. 2d 83. In that case the United States inadvertently paid the Trustee in Bankruptcy refunds for taxes in the amount of approximately $35,000.00. At that time the United States had on file a proof of claim for $24,000.00, which proof of claim recited, among other things, that there were "no set-offs or counterclaims". An amendment of the claim was filed after the period for filing claims had expired. The question was whether the amendment of the proof of claim made in the month following its filing, and after the expiration of the statutory period for the filing of claims, was valid. The court held that it was, inasmuch as no one "had changed his position to his detriment in reliance on the previous failure to state the facts" (207 F. 2d at p. 83). The observation was made in the opinion that the allowance of the amendment did not turn on the fact that the claimant was the United States.

In the case before this court, it is apparent that the conclusion that the Bank waived the right of set-off is wrong.

Proposition III.

The Bankrupt's account was a general commercial account subject at all times to its unrestricted order. It was not at any time a special deposit or trust fund, nor did it partake of any of the characteristics of either.

Zollman, Banks and Banking, Vol. 5;
Michie, Banks and Banking, Vol. 5 b;
Union Bank & Trust Co. of Helena, Montana, vs. Loble, 9th Circuit, 1927, 20 F. 2d 124;
Citizens National Bank of Gastonia vs. Lineberger, 4th Circuit, 1930, 45 F. 2d 522;
Killoren vs. First National Bank in St. Louis, 8th Circuit, 1942, 127 F. 2d 537;
Craig vs. Bank of Granby, 1922, 210 Mo. App. 334, 238 S.W. 507.

A deposit in a bank is presumed to be a general deposit, and the burden is on him who would seek to establish otherwise to rebut the presumption.

Zollman, Banks and Banking, Vol. 5, Sec. 3156, 3593;
Michie, Banks and Banking, Vol. 5 b, Sec. 328;
Killoren vs. First National Bank in St. Louis, 127 F. 2d 537.

Where a depositor has had a long history of general deposits and has maintaind a general account, there must be a clear and explicit direction by the depositor accepted by the bank to effect a change of the deposit from a general account to a special account.

Zollman, Banks and Banking, Sec. 3156;
Michie, Banks and Banking, Sec. 328 and 330.

The fact that an account is subject to the unrestricted drawing by check by the depositor is evidence that it is a general account.

Michie, Banks and Banking, Sec. 334;
Killoren vs. First National Bank in St. Louis, 127 F. 2d 537.

Inasmuch as the Bankrupt's account was a general commercial account in its inception and continued as such during its entire existence, the burden was, and is, on the Trustee to show wherein it was changed. The Trustee did not discharge this burden. The undisputed finding of fact of the Referee is that the Bankrupt opened a general commercial account with the Bank in 1946 and that it "continued in existence without change except as to the amount thereof, to and including the date of the exercise by said Bank of its asserted right of offset" (Transcript of Record, page 19). There is not a scintilla of evidence to the contrary. Appellant's Exhibit 5 (Transcript of Record, page 61) shows a consistent pattern of unrestricted withdrawals until the account was finally closed in July of 1953. Mr. Lynn, Vice President of the Bank and Manager of the Branch at which the Bankrupt's account was maintained, testified that the nature of the account remained unchanged from its inception and that it was always absolutely subject to the order of the Bankrupt (Transcript of Record, pages 60, 62). The account was in all respects the same as any other general commercial account.

In the case of *Union Bank & Trust Co. vs. Loble,* 1927, 20 F. 2d 124, which is more fully discussed later in this brief, this Court held that the account there, also denominated by the parties as a general commercial account, had acquired the characteristics of a trust fund. Although the account was called a general commercial ac-

count, it was not in fact, inasmuch as at the inception of the account limitations were placed on the right of the depositor to withdraw from it. It was created by agreement between the parties to receive the proceeds of a special sale to be held by the bankrupt. Under the agreement, the funds could only be used to pay current expenses and certain eastern creditors. They could not be used to pay certain local creditors. This court rightly held that the Bank could not divert the funds in a manner contrary to the agreement. The distinction between the *Loble* case and the case before this Court, where the account was in all respects a general commercial account unrestricted in any way, is apparent.

In *Citizens National Bank of Gastonia vs. Lineberger,* 1930, 4th Circuit, 45 F. 2d 522, a set-off was allowed under the following circumstances:

The Kirby-Warren Company, hereafter called "Company", found itself in financial difficulty in March of 1927. On March 12th Messrs. Kirby and Warrent, the sole officers and stockholders of the Company, and personally solvent, met with the president of the plaintiff bank, who was the brother-in-law of Kirby, and their attorney, who was a director of the bank and a member of its finance committee. The Company owed the bank some $14,700.00. It was decided at this meeting to write a letter to all creditors offering to compromise the claims of the Company for 25% of their face value, and to call a meeting for March 24th to consider this proposal.

On March 14th the bank collected $2100.00 on a $4500.00 overdue note, of which Kirby was an endorser.

$600.00 of this collection was the balance in the Company's account and $1500.00 was the proceeds of a loan obtained by Kirby from the bank which he used to pay his indebtedness of $1500.00 to the Company. The Company in turn used this money to pay the Bank.

The Bank continued to accept deposits by the Company in its general account and continued to honor checks drawn by the Company on this account throughout the month of March. On April 1, 1927, the Company filed a voluntary petition in bankruptcy and on the same date the bank set off the balance in its account, which had all been accumulated during the month of March, against the indebtedness owing it. The court held, in a well-reasoned opinion, that the collection of the $2100.00 was proper and that the set-off of the balance in the account was proper. With reference to the contention that the deposits made during the month of March were a trust fund, the court had the following to say at page 531 and following:

> "We have carefully considered the trust fund theories urged by the learned counsel for the trustee, but we do not think that they are applicable. If the letter to creditors had promised that moneys collected should be kept segregated and should be deposited in a special account for the benefit of creditors, an express trust would have arisen which could have been enforced against the bank if it had had notice of the trust. The letter, however, promised merely that the assets of the company would be protected and preserved in the interest of creditors pending consideration of the offer of compromise, which falls far short of the language necessary to create a trust. As a matter of fact, it promised nothing except what the law required in the absence of promise.

> "It is true that the assets of an insolvent corporation which has suspended business constitute a trust fund for the benefit of its creditors; but in the case at bar the company did not suspend business until April 1st, after the deposits in question had been made, and after the right of set-off on the part of the bank had accrued . . . Even though a corporation be insolvent, it does not lose the right of doing business in the ordinary way with a bank, nor does a bank in doing business with it relinquish any of its ordinary rights or remedies. If there were showing that the deposits in question were made fraudulently or collusively, as a cloak for payments to the bank or as a means of giving it security, the trustee could avoid them under the Bankruptcy Act, without resort to the trust fund doctrine, if the bank were shown to have been a party to the fraud or collusion, or to have accepted the deposits as a means of obtaining payment or security."

In the case before this Court there was never any agreement, express or implied, that this account was intended to be a trust fund, or restricted in any manner. It was the sole property of the Bankrupt. There was never any restriction of any kind on the Bankrupt's right to withdraw from it. It was not designated to be used for any special purpose and it had none of the characteristics of a trust fund. It was a general commercial account subject to all the rules applicable thereto, as specifically found by the Referee in his Findings of Fact.

If under such circumstances it is to be held that the Bank had no right of setoff, then it is difficult to imagine a situation in which such right exists, unless this court is to hold, as a matter of law, that, in order to preserve its right of set-off, a bank must refuse to grant any ex-

tensions of time or other indulgence or to cooperate with a debtor in any respect. Such a rule would be contrary to law and the decisions of our courts, would tend to increase greatly the number of bankruptcies and would result in conditions exactly contrary to those which are admittedly to the best interests of all of the interested parties, particularly the debtor.

Killoren vs. First National Bank in St. Louis, 1942, 8th Circuit, 127 F. 2d 537, is of particular interest because, on facts substantially more in favor of the adoption of the "trust fund theory" than those presented in the case before this Court, the court held, decisively, that there was no trust fund. The suit was brought in equity by the trustee of the Hamilton-Brown Shoe Company, hereafter called the "Company", to impress a trust upon the funds of the bankrupt in the hands of the First National Bank of St. Louis, hereafter called the "Bank". The Trustee alleged that the Company had deposited approximately $27,000.00 in its account with the Bank for the specific purpose of meeting its payroll. The deposit was made on April 14, 1939. On April 17, 1939, the Bank set off the balance in the account against the indebtedness owing from the Company to it. The Bank denied that any special deposit was made, and the court so found. It was held that the set-off was proper. At page 542, the court made the following observations:

> "Not only did the depositor in the instant case not indicate an intention to create a trust or a special deposit subject to use for a specific purpose, but the evidence shows that the bank did not understand that the depositor intended so to do, or that it intended to enter into any special relationship. Noth-

> ing was done to indicate that the relationship of debtor and creditor which had before existed was to be changed into a different relationship."

The observation made by the court in the case of *Killoren vs. First National Bank in St. Louis* is particularly appropriate to the case now before this Court. There is nothing in the findings of fact or in the record to indicate that the relationship of debtor and creditor, which had existed since the establishment of the account, was to be changed; or that the funds then or thereafter credited to the account were subject to any restrictions or understanding of any kind. We earnestly submit that the conclusion of the Referee, affirmed by the District Judge, that the account bore the characteristics of a trust fund is without factual support and is contrary to law.

Proposition IV.

The case of *Union Bank & Trust Co. of Helena, Montana vs. Loble,* 9th Circuit, 1927, 20 F. 2d 124, does not constitute any authority or justification for the denial of the Bank's right of set-off in this case.

The Trustee has contended that the case presently before this Court is so similar to *Union Bank & Trust Co. of Helena, Montana vs. Loble,* 20 F. 2d 124, decided by this Court in 1927, as to be controlled by it. For convenience, the case will be referred to as the "Loble" case.

The facts in the Loble case as found by the District Court and reported in 14 F. 2d at page 116 are as follows:

"The evidence is that early in December, 1925, the bankrupt owed the bank $10,000 upon a 90-day renewal note and $1,300 upon an overdraft, owed $35,000 to relatives of its president manager and $16,000 to Eastern supply houses, was without funds, insolvent, pressed by creditors, suspension of business imminent, and in extremis. Thereupon its president-manager was ousted by Loble, son of the principal creditor relative, and various conferences followed between Loble, for the bankrupt, and McKinnon and Bogart, for the bank.

"The outcome was an agreement that the relatives and bank would refrain from pressing their claims, an extraordinary sale of the bankrupt's stock in trade would be had, and the proceeds would be deposited in the bank and devoted to payment of urgent Eastern creditors, all in the hope and to the end that continued credit and supplies might be secured, solvency restored, and all creditors finally paid. Despite some conflict in details, there is none that *the plan was the bank's and the agreement made upon its insistence.* This agreement was so far executed that the sale was had, and thereafter and to January 25, 1926, when the voluntary petition for adjudication was filed, the deposits served to extinguish the overdraft, to pay some $6,000 of the bankrupt's checks for current expenses and other accounts, and to accumulate a residue of $8,378.56, which on the date last aforesaid the bank applied in payment upon the bankrupt's note aforesaid. (emphasis added)

"In the meantime, however, the bank had refused to permit the use of the deposits to pay the Eastern creditors, and none such were paid; that is to say,

> *the bank repudiated the agreement, the contract by which alone the bankrupt's assets were converted into money and deposited with the bank."* (emphasis added)

This court, in accepting the facts as found by the referee and affirmed by the district court, made the following statement: (20 Fed. (2d) at p. 125)

> "Accepting the relevant facts as found by the referee and affirmed by the District Court, the case here presented is, in brief, one in which the bankrupt, upon consultation with the bank and acting upon its advice, made a special sale of merchandise to raise money for the purpose of paying demands of Eastern creditors, and facilitating the continuation of the bankrupt business, in the expectation of reorganizing the same under an arrangement whereby relatives to whom the bankrupt was indebted were expected to take stock therein."

After observing that there was no evidence that the bank advised the holding of the special sale with the view to obtain a preference, this court continued as follows: (20 Fed. (2d) p. 125)

> " . . . While the money was in its (the bank's) possession on deposit, the bank placed no obstacle in the way of its disbursement to Eastern creditors until early in January, when it became apparent that the suggested plan of reorganization had failed. Thereafter the bankrupt presented to the bank a proposition to compromise with all creditors on the basis of 25 cents on the dollar. The bank denied the bankrupt's right thus to use the money on deposit, and asserted its own claim of lien thereon. On the following day the bankrupt filed its voluntary petition in bankruptcy." (parenthesis added)

Following is an outline comparison of the facts in the Loble case as reported by the District Court in 14 F. 2d

at p. 116 and by this Court in 20 F. 2d at p. 124, and the undisputed facts in this case as found by the Referee:

Loble case	*This case*
1. At the time of the agreement the Bankrupt owed the Bank $10,000 on a 90-day renewal note. It is not stated whether the note was in default.	1. At the time the extension was granted the Bankrupt owed the Bank $20,000 on a note which was in default.
2. The Bankrupt not only had no balance in its account, it was indebted to the Bank on an overdraft in excess of $1,000.	2. The Bankrupt had a balance in its account ranging from $8165.79 to $22,301.09 during December, 1952. The exact date of the discussion between the representatives of the Bankrupt and the Bank is not in the record.
3. After a series of conferences initiated by the Bank, a plan formulated and presented by the Bank was adopted at the insistence of the Bank, resulting in an agreement between the Bankrupt, the Bank and creditor-relatives of the Bankrupt's management.	3. The Secretary-Treasurer of the Bankrupt and its attorney called on an officer of the Bank to advise him of the Bankrupt's financial condition. They suggested that if the excessive inventory were liquidated in the normal course of business, rather than as salvage stock, they thought the corporation would be able to continue its operation. They suggested that the Bankrupt make quarterly payments to its creditors of its outstanding obligation. The Bank stated that quarterly

	payments would not be acceptable, but that if the Bankrupt made payment in liquidation of its obligations owing the Bank of 10% per month commencing in January 1953, the Bank would defer any action on the obligation, but only for so long as the monthly payments were made.
4. The agreement between the Bankrupt, the Bank and the creditor-relatives was: (a) To have an extraordinary sale; (b) The proceeds of the sale to pay "urgent Eastern creditors" (14 F. 2d 117). The purpose of the sale was to create a particular fund for a particular purpose. (c) To deposit the proceeds of the sale in the Bank.	4. There was no agreement in the sense the term was used in the Loble case. The Bank granted an *extension of time* to the Bankrupt within which to liquidate the obligation, expressly conditioned on the prompt payment by the Bankrupt of 10% of the obligation each month commencing January 15, 1953. The extension agreement did not earmark the deposit for any particular purpose.
5. At the date of the exercise of the right of set-off, the Bankrupt's account had increased from approximately a $1,000 deficit to an $8,378.56 credit.	5. At the date of the exercise of the set-off, the Bankrupt's account had decreased from a sum between $8,000 and $22,000 to $2,889.14.
6. A fund was created by the operation of the agreement.	6. An existing fund was depleted during the liquidation program adopted by the Bankrupt.
7. The Bank refused to allow the funds to be used	7. The Bankrupt failed to comply with the condition

to pay Eastern creditors, as contemplated by the agreement, (14 F. 2d 117) apparently because the Bankrupt had presented an alternative plan to it involving the payment of 25% to each creditor. (20 F. 2d 125) The Bank breached the agreement by diverting the funds in the account (which had been created for a special purpose) to its own use, contrary to the agreement.	on which the extension of time was granted by not making the June payment, and by filing its voluntary petition in bankruptcy.
8. The Bank asserted the setoff before the petition in bankruptcy was filed.	8. The Bank exercised the set-off after the petition in bankruptcy was filed.
9. The account was created for a specific purpose and the bankrupt was expressly limited by the agreement between the parties from making any withdrawals from it except as authorized by the agreement.	9. The account was created some six years prior to the financial difficulty of the Bankrupt and continued until the right of set-off was exercised. As specifically found by the Referee, there was no change of any kind in the account or the manner in which or the terms upon which it was operated or maintained. The extension agreement did not provide that the future deposits should be used for any specific purpose.

The distinction between the cases is apparent. In the Loble case the fund against which the right of set-off was exercised was created by the operation of an agree-

ment formulated by and adopted at the insistence of the Bank and with which agreement the bank ultimately refused to abide. In this case a substantially larger fund, perhaps sufficiently large to completely eliminate the indebtedness owing the bank, was in existence on the date the extension was granted and was at that time subject to the exercise by the Bank of its right to set-off. The plan, to the extent that it was a plan, was developed by the Bankrupt and the only thing that the Bank did was to agree to extend the maturity of its own note as long as the stipulated installments were paid at the times and in the manner designated. If such an extension of time constitutes a waiver of a right of set-off, then it necessarily follows that the only manner in which a bank can preserve this right is to exercise the right at the first opportunity regardless of the consequences!

The courts have consistently regarded the Loble case as advancing the proposition that a creditor that requires the adoption of a plan formulated by it, the result of the operation of which plan *creates* a fund *earmarked for a particular purpose* and which fund, except for the operation of the plan, would not have been created, cannot thereafter be permitted to appropriate that fund to its own purposes and for its own benefit. It is quite apparent that this proposition is a correct one. But it is not a correct statement of the law to say that any agreement to defer the collection of an obligation that is due and owing, no matter upon what terms the agreement may be conditioned, is an absolute waiver of the right to enforce collection of that obligation. Nor does the Loble case so hold.

It is equally clear that none of the elements of a trust fund are here involved because there was never any understanding to apply the depositor's account for any specific use.

The Ninth Circuit, the Court which decided the Loble case, advanced this interpretation of this case in *Ingram vs. Bank of Cottage Grove,* Or. 1928, 29 F. 2d 86. In explanation of the Loble case, the court said, at page 87:

> "True, it was held in the Loble Case that the bank waived, or was estopped to assert, its right of set-off, because of an agreement between the bank and the bankrupt that certain moneys derived from a special sale conducted by the bankrupt and placed on deposit in the bank should be paid to certain eastern creditors, but there is no basis for any claim of waiver or estoppel here."

It is important to note in the case before this Court that there was no agreement of any kind that the Bankrupt's account should in any way be affected by the agreement between the Bankrupt and the Bank. On the contrary it is the express finding of the Referee at paragraph 7 of the Order Disallowing the claim (Transcript of Record, page 19) that:

> "7. That in 1946 the bankrupt opened with The First National Bank of Portland a general commercial account in which unrestricted deposits were made subject to withdrawal by check in the ordinary course of business. This account was in existence at the time of the creation of the loan upon which the claim of the Bank is based and continued in existence without change, except as to the amount thereof, to and including the date of the exercise by said Bank of its asserted right of offset. The activity

> in the account and the high and low monthly balances for the period from January, 1951, through June, 1953, are shown in Exhibit 5, which is included by reference herein as a part hereof. The deposits in and withdrawals from the account and the balances after each daily transaction in the account for the period of from November 29, 1952, until the account was closed, are shown in the copies of the bank statements which are Exhibit 6, and which is included by reference herein as a part hereof."

The Bankrupt's account was not in any way changed nor was any restriction of any nature placed on its right to use the funds for any purpose it saw fit. There is certainly no analogy between this state of facts and the explanation given by the Ninth Circuit in the Ingram case of its decision in the Loble case that the bank "waived, or was estopped to assert, its right of set-off, *because of an agreement between the bank and the bankrupt that certain moneys derived from a special sale conducted by the bankrupt and placed on deposit in the bank should be paid to certain eastern creditors* . . . " (29 F. 2d 87 — emphasis supplied).

The Ingram case is of further interest because the court there held that the bank was entitled to exercise its right of set-off on a state of facts which we submit is less favorable to the bank than are those presented in this case. In that case the bankrupt operated a general merchandise business in Cottage Grove. On June 22, 1927, he was heavily involved and went to Portland for the purpose of conferring with the Portland Association of Credit Men. After some discussion, it was agreed that a note secured by a mortgage on his stock should be

executed by the bankrupt pending efforts to obtain an extension of credit from his creditors, the extension to be until January 1, 1928. A note and mortgage were executed, but for some reason the indebtedness due the bank of Cottage Grove was not included; and it was not until June 28th that the bank was advised of what had happened. The president of the bank and the manager of the Bureau had some discussion in which the bank indicated it did not favor the existing arrangement and during which such discussion it was agreed that the bank president should go to Portland to discuss the matter further.

Nothing further was done until July 22nd. From June 22nd until July 22nd the bankrupt made deposits in the amount of about $2100.00 and drew checks in the usual course of his business in the amount of about $1300.00. On July 22nd, immediately prior to leaving for Portland, the president of the bank directed the Cashier to charge off $600.00 of the amount on deposit as a set-off of the amount owing the bank. On July 25th and additional $150.00 was set off.

The Referee found that the Bank was entitled to set off the $600.00, but was not entitled to set off the $150.00. The trustee appealed the allowance of the $600.00 set-off. The bank did not appeal the disallowance of the $150.00 set-off. The decision of the Referee in allowing the $600.00 set-off was approved by the District Judge and affirmed by the Circuit Court.

After a recital of the foregoing facts, the court continued as follows (29 F. 2d p. 87):

"From the facts as found by the referee and approved by the District Judge, the deposits in the appellee bank were made by the bankrupt from time to time in the ordinary course of his business, and were checked out by him in the same manner. The deposits were not made for any specific purpose, nor were they subject to a trust of any kind. There was no fraud or collusion between the bankrupt and the bank, and it does not appear that the deposits were made for the purpose of enabling the bank to gain a preference. Under somewhat similar facts in Union Bank & Trust Co. v. Loble (C.C.A.) 20 F. (2d) 124, this court said:

" 'The balance of a regular bank account at the time of filing the petition in bankruptcy is a debt due to the bankrupt from the bank, and in the absence of fraud or collusion between the bank and the bankrupt, with the view of creating a preferential transfer, the bank need not surrender such balance, but may set it off against the bankrupt's debt to it.'

"We there quoted with approval from In re Almond-Jones Co. (D.C.) 13 F. (2d) 153, as follows:

" 'The question then arises whether the bank was justified in applying the moneys deposited after it had knowledge of the company's insolvency to the payment of its note. The solution depends upon the purpose with which the deposits were made and accepted—whether they were made in the ordinary course of business, with the expectation and intent that they might be withdrawn at will by the bankrupt, or whether, on the other hand, they were made to build up the account, so that it would be applied to the payment of the bank's claim . . . In these cases it is laid down that, in the absence of fraud or collusion between the bank and the depositor, with a view of creating a preferential transfer, the bank need not surrender the balance in the bank account at the time of the filing of the depositor's petition in bankruptcy, but may set it off against the deposit-

or's indebtedness and prove its claim for the amount remaining due.'

"True, it was held in the Loble Case that the bank waived, or was estopped to assert, its right of set-off, because of an agreement between the bank and the bankrupt that certain moneys derived from a special sale conducted by the bankrupt and placed on deposit in the bank should be paid to certain eastern creditors, but there is no basis for any claim of waiver or estoppel here.

"The order is therefore affirmed."

The limitation of the Loble case to the state of facts where a fund is created by a plan formulated by and adopted at the insistence of the creditor and thereafter appropriated by the creditor in a manner and for a purpose contrary to the plan is further recognized by the Eighth Circuit in the case of *Killoren vs. First National Bank of St. Louis,* 1942, 127 F. 2d 537. There the court made the following reference to the Loble case, beginning at page 543:

"In Union Bank & Trust Co. of Helena v. Loble, supra, the bankrupt owed \$16,000.00 to Eastern supply houses, owed relatives of its president \$35,000, and owed local creditors \$12,000. It was also indebted to the bank in the sum of \$10,000 on a ninety-day note and in the sum of \$1,300 on an overdraft. It was insolvent and without funds. The bankrupt discussed with the president of the bank the question of discontinuing the business, but upon the bank's advice it was agreed that a special sale should be conducted by the bankrupt to raise money to pay Eastern creditors, with a view of reorganizing and continuing the business, and that the relatives and the bank would refrain from pressing their claims. The court found that this plan was the bank's own plan and the agreement above referred

> to was made upon the bank's insistence. Pursuant to this plan the sale was held and the proceeds turned into the bank. The bank paid out about one-third of the money realized from the sale, but none of it was used to pay the Eastern creditors, but was used largely to pay some of the local creditors who were relatives, and to pay current expenses and the bank's overdraft of $1,300.00. There was a residue of about $8,300 on the date a voluntary petition in bankruptcy was filed, and on the same date the bank applied this balance on its note. The trial court held that the deposit was in the nature of a special deposit brought about by the bank under an agreement that it was to be devoted to certain purposes, and that, 'By breach of contract a trust cannot be converted to a debt, the title to special deposits cannot be transferred, and set-off against them cannot be had by the defaulting contractor.' In re Gans & Klien, D.C., 14 F. 2d 116, 117. The Circuit Court of Appeals, 9 Cir., 20 F. 2d 124, 126, in affirming the lower court, expressed the view that, ' . . . the circumstances under which the fund was created, and the co-operation of the bank and the bankrupt in its creation were sufficient to so far impress upon it the character of a trust fund that the bank should be held estopped to assert a lien thereon or the right of set-off.' "

In the Killoren case, the plaintiff was trustee of the Hamilton-Brown Shoe Company, hereafter referred to as the "bankrupt". On April 14, 1939, the bankrupt deposited with the defendant about $27,000.00, about $26,000.00 of which represented a loan obtained by the bankrupt from the Commercial Factors Corporation, hereafter referred to as the "corporation", for the specific purpose of meeting a payroll of the bankrupt. There was some evidence that the defendant knew that the deposit was for this specific purpose.

About $8,000.00 of the account was checked out by April 17, on which date the bankrupt filed its voluntary petition in bankruptcy and the defendant set off the remaining $19,000.00 in the account against the bankrupt's indebtedness owing it.

The plaintiff trustee appealed from a judgment dismissing its complaint on the grounds:

> " . . . (1) That the bank had no right of set-off because it knew, or by reasonable investigation could have ascertained, the purpose of the deposit; (2) That the bank had no right of set-off even though without knowledge that another than the depositor had an interest in funds deposited in its name, where such lack of knowledge has not resulted in any change of the bank's position and if no superior equities have been raised in its favor; (3) That the right of set-off should not be allowed because to do so would give the bank a preferential advantage over other creditors."

The court found that there was no agreement between the defendant and the bankrupt or the corporation that the $27,000.00 deposit was to be used as a separate deposit, but to the contrary that it was deposited by the bankrupt with the defendant in the regular way, in the regular checking account, that it was subject to check by the bankrupt in the regular way, and that there had been no agreement, express or implied, that the account, including the $27,000.00, should not be drawn against in the usual course of business.

The court overruled plaintiff's contentions and held that the defendant had rightfully exercised the right of set-off. The court also observed that this was not a trust fund. There was no indicated intent on the part of the

depositor to create a trust fund or to create a special deposit, or on the part of the defendant bank that such a deposit be created. Nothing was said or done to change the then existing debtor-creditor relationship. The court concluded its opinion with the quotation hereinabove on page 36 hereof set forth.

In the case of Citizens National Bank of Gastonia vs. Lineberger, 1930, 4th Circuit, 45 F. 2d 522, which case was more fully discussed under Proposition III of this brief, the court regarded the Loble case as holding that, because a special deposit had been created, the bank was estopped to assert its right of set-off. The court there stated, at page 530:

> "In Union Bank & Trust Co. vs. Loble (C. C. A. 9th) 20 F. (2d) 124; Id. (D. C.) 14 F. (2d) 116, the deposits made were proceeds of a special sale, held on the advice of the bank, to raise funds for Eastern creditors. It was held that the circumstances under which this fund was created and the co-operation of the bank and the bankrupt in its creation so far impressed it with a trust as to estop the bank from asserting its right of set-off."

The same emphasis was made by the Fourth Circuit in the case of Twentieth Street Bank vs. Gilmore, 1934, 71 F. 2d 594, where it observed that the Loble case was one " . . . where the deposits were the proceeds of a sale to raise funds for Eastern creditors, and it was held that the circumstances under which the funds deposited were raised and the cooperation of the bank with the depositor so far impressed them with a trust as to estop the bank from asserting its right of set-off".

The foregoing are the only cases of which we are advised where the Loble case has been cited and particular reference made to the nature of the case. It is clear that each of the courts, including this court, regarded the Loble case as one where the peculiar combination of a plan formulated and adopted by and at the insistence of the creditor caused the creation of a fund designed to be used for a particular purpose and to which the creditor should not be allowed to look for payment of its own obligation contrary to that purpose. None of these facts which have been regarded by all of the courts as being controlling in the Loble decision is present in this case. Contrary to the contention of the Trustee that the Loble case requires that the Bank in this case be denied its right to exercise the set-off specifically granted it by the statute and the cases, the Loble case requires that the right of set-off be allowed on the facts as found by the Referee.

CONCLUSION

When this matter was before the District Court, counsel for the trustee argued that an extension of time within which to pay a delinquent obligation operates as an absolute waiver of the right to proceed to the collection of the obligation for the duration of the extension, even though the extension is conditioned upon periodic payments on the delinquent obligation; and that the only way that the rights which the creditor had at the time the extension was granted could be retained was by *express reservation*. A conditional extension, such

as was granted in this case, is, according to the trustee, insufficient. We know of no law supporting such a statement. It is contrary to all the law of waiver and estoppel.

The effect of the trustee's argument is to create in the delinquent debtor who has obtained a conditional extension of time within which to pay his obligation, greater rights than he would have had if he had not allowed his debt to become delinquent; and this would be true even though the debtor did not keep the condition on which the extension was granted. Such a contention is preposterous.

If the Bankrupt's obligation in this case had been in a current condition, there would be no question but that the Bank would have had the right of set-off, and the exercise of this right would have gone unchallenged. But, because the debtor became delinquent and because the Bank granted an extension expressly conditioned upon regular periodic payments of the delinquent balance in liquidation of the debt, which condition was not kept by the debtor, it is asserted that the Bank is barred from exercising the right it concededly would have had if the obligation had been in a current and unmatured condition. None of the elements of waiver is present. None of the elements of estoppel is present. None of the elements of a trust fund or special deposit or quasi fiduciary relation, or of basic inequity, such as are in the Loble case, is present. The facts are not in any sense extraordinary or unusual. The question presented to this Court is whether a simple garden variety conditional extension of time within which to pay a delinquent obligation

operates as an absolute bar to the subsequent exercise by the creditor of the right of set-off, even where the condition has not been kept by the debtor. The simple answer to this proposition, when so presented, is that such a conditional extension of time is not a bar. It is the only answer.

The Honorable District Judge before whom this matter was heard on review asserted that he was " . . . not impressed as an original proposition that such a loose arrangement, as presented here, should work a loss of the Bank's right of set-off . . . " (Transcript of Record, page 27). It was the court's feeling, as evidenced by the Memorandum of Decision, that, inasmuch as the Referee regarded this case as being controlled by the Loble case, it would not be inappropriate for this Court, which decided the Loble case, to point out wherein the two cases may be distinguished. We feel it not inappropriate, also, to add that it was the suggestion of the Honorable District Judge that the whole record be submitted to this Court that caused us to have the transcript of testimony printed as a part of the printed record, even though the Findings of Fact as made by the Referee were not, and are not, contested.

We submit that, if the decision of the Referee is supported, a financially embarrassed person, whether corporate or individual, cannot look to a bank, or indeed to any creditor who is also a debtor, for an extension of time within which to attempt to work out his problem, or for any other assistance. A creditor would have no alternative but to deny the extension, or other assistance,

and exercise its then existing right of set-off; for by not so doing, he would be held to have lost that right, irretrievably, and without regard to whether any of the elements of waiver, estoppel, trust fund or similar special circumstances were present. This would obviously precipitate many bankruptcies which might otherwise be avoided. It would produce evils of a much more serious and far reaching consequence than were within the contemplation of the Supreme Court of the United States in 1913, when the case of Studley vs. Boylston National Bank of Boston, supra, was decided. It is patently wrong, and the cases unanimously so hold. The order of the District Judge is erroneous and should be reversed.

Respectfully submitted,

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